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C O N F I D E N T I A L SECTION 01 OF 04 TOKYO 000548

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TAGS: [PGOV](#) [EFIN](#) [MARR](#) [JA](#)

SUBJECT: DECISION TIME IN DIVIDED DIET OVER BUDGET, BANK OF
JAPAN APPOINTMENT

REF: A. TOKYO 0235
[1](#)B. TOKYO 0142

Classified By: Ambassador J. Thomas Schieffer, reasons 1.4(b),(d).

[1](#)1. (C) Summary. The final outcome of intense Diet debate over the budget, budget-related bills, and the appointment of a new Bank of Japan (BOJ) Governor remains murky as key deadlines approach. Six weeks into the Diet session, the opposition DPJ has managed to block progress on deliberations, using several highly-publicized scandals and other unfortunate incidents to keep the government on the defensive. The government intends to bring the budget to a vote in the Lower House on February 29, aiming to enact it by the time the new fiscal year opens on April 1. The Lower House will also vote February 29 on the controversial Special Tax Measures Law revision. This and other budget-related bills, while separate from the budget, also expire at the end of the fiscal year. One budget-related bill that may directly impact the U.S. government if delayed past April 1 is the Special Measures Agreement governing USD 1.2 billion in Host Nation Support for U.S. forces in Japan. The opposition is threatening to respond to coalition party budget action by blocking the appointment of a new BOJ Governor to take over when the incumbent's term expires on March 19. End summary.

Sagging Support for Fukuda's Low-Key Approach

[1](#)2. (C) Six weeks into the Diet session, the ruling Liberal Democratic Party (LDP)-Komeito coalition is still struggling to resolve the three key issues that were expected to dominate the first ten weeks of the session -- the budget, budget-related tax legislation, and key appointments to the Bank of Japan (BOJ). Press reports and Embassy contacts alike place some of the blame for this lack of progress on the cautious, consensus-oriented management style of Prime

Minister Yasuo Fukuda. Polls show Fukuda's lack of leadership skills is a key factor in his dropping support rate. The Prime Minister's public support has dropped from highs in the upper 40s and low 50s at the beginning of his term in late September 2007 to the upper 20s and low 30s today, with non-support approaching or exceeding 50 percent in nearly every major poll.

High-Profile Scandals Help Conceal DPJ Disunity

13. (C) Fukuda has been buffeted by a number of troubling incidents in recent weeks, including the discovery of tainted food products from China, an alleged rape and other misconduct by U.S. military personnel in Okinawa, and a fatal collision involving an Aegis-equipped Japanese Maritime Self-Defense Forces vessel and a fishing boat. These incidents, along with questions over their handling by the government, have given the main opposition Democratic Party of Japan (DPJ) ammunition to delay deliberations in the divided Diet and to frustrate progress on Fukuda's legislative initiatives, much as the DPJ used defense-related scandals to block movement on the Indian Ocean refueling bill in the 2007 Diet session.

14. (C) While Fukuda has faced down DPJ threats of a censure motion, pressure is mounting to take action with respect to a purported cover-up at the Ministry of Defense over the Aegis/fishing boat accident. Fukuda insists that he will not seek Defense Minister Ishiba's resignation, but DPJ leaders say the opposition is ready to link Ishiba's fate to action on the budget-related bills and the appointment of the new

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Bank of Japan governor.

15. (C) The DPJ has not presented a united front. A number of senior DPJ lawmakers have gone public recently over policy disagreements with DPJ leader Ichiro Ozawa, and the party has yet to come through with either a counterproposal to the ruling coalition's budget-related bills or a clear slate of nominees for the BOJ, despite repeated requests from the ruling parties and the press. Embassy contacts within the DPJ note a continued lack of cohesion among different elements of the party, and simmering discontent over Ozawa's one-man management style.

Budget Passage Could Come With a Price

16. (C) Passage of the FY2008 budget is the most time-sensitive issue on the agenda at the moment, but also the easiest to solve. In accordance with the Constitution, the budget is considered approved 30 days after passage in the Lower House, regardless of subsequent action by the Upper House. The government thus plans to put the budget to a vote in the Lower House late in the day February 29, to ensure the budget's passage by the time the new fiscal year opens April 1. Legally, the opposition is powerless to block the budget, even if it boycotts deliberations or passes a censure motion. Practically speaking, however, control of the Upper House has proven a powerful lever for the opposition since elections last July. In the case of the budget, the DPJ is threatening to take measures to delay budget-related bills and the BOJ appointment, if not given more time for deliberation. This contrasts with the supplemental budget for FY2007, which passed the Lower House with mostly bipartisan support on January 29, and became law February 6.

Budget-Related Bills More Problematic

17. (C) Budget-related bills, too, need to move quickly through the Diet, if the government is to avoid the sunset of key tax measures on March 31. The government has proposed a bill encompassing all proposed national tax changes,

including provisions to extend a number of Special Tax Measure Laws that will expire at the end of the fiscal year, such as controversial gasoline-related taxes and surcharges. Many of these laws contain multiple provisions affecting a variety of interests and constituencies. The Special Tax Measures Law alone accounts for 110 separate revenue items. Provisions related to tariffs on beef and corn could prove particularly significant for U.S. agriculture, if the legislation is not revised and extended by the deadline. LDP contacts have stressed that the government does not want to be seen as imposing new taxes after April 1, if the existing taxes are allowed to lapse. The government plans to debate and vote on the Special Tax Measures Law revisions February 29 and early March 1.

18. (C) Unlike the budget itself, budget-related bills can be held in the Upper House for up to 60 days, after which they can be passed into law by a two-thirds re-vote in the Lower House. The government has already passed the deadline required to prevent the taxes from lapsing on April 1, relying on a January agreement brokered by Lower House Speaker Kono and Upper House President Eda to reach "a certain conclusion" on the measures before the end of the fiscal year. The problem is that from the beginning, neither party appears to have had a clear understanding of what they agreed to, or a concrete plan for realizing the agreement. Former Special Advisor to Prime Minister Abe Hiroshige Seko told the Embassy that the LDP had given up passage of a

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stopgap "bridging" bill in exchange for DPJ promises to vote the budget-related bills up or down before the end of March, allowing the ruling coalition to exercise its override, if necessary. LDP Lower House member Kenji Kosaka noted the need to exercise care in over-using the two-thirds re-vote, however, to avoid the appearance of a "dictatorship" of the ruling parties.

Road-Related Tax Reform

19. (C) DPJ leaders want to integrate all road-related taxes into general revenue. The ruling parties have indicated they are amenable to considering a revised bill in the Upper House, based on a DPJ counterproposal, but the opposition is not ready with its own legislation, according to DPJ staffers. A senior media contact told the Embassy he believes a compromise can be reached if the LDP and DPJ can agree to shorten the extension period, increase the percentage of road-related taxes to be used as general revenue, and convert a portion of the proceeds to use for the environment.

SMA Delays Could Impact U.S. Training

110. (C) There is one budget-related bill that may impact directly on the U.S. government if delayed past April 1 -- the Special Measures Agreement (SMA) governing USD 1.2 billion in Host Nation Support (HNS) for U.S. forces in Japan. MOFA and Ministry of Defense (MOD) officials tell the Embassy that the bill is unlikely to clear the Lower House until mid-March. The Upper House is likely to drag out debate for the full 30 days, leaving a gap of more than two weeks. The delay will not affect salaries for local base employees or reimbursements for on-base utilities, categories that account for all but USD 18 million of the total SMA. However, MOD has warned that the delay could slow Japanese-funded training relocation scheduled for April (Septel).

New Bank of Japan Governor Hostage to Budget Debates

111. (C) The government is expected to nominate Deputy Governor Muto of the Bank of Japan to succeed Governor Fukui

when he steps down on March 19. Muto enjoys solid support among many DPJ lawmakers, who acknowledge his strong credentials to lead the BOJ during a period of world-wide economic uncertainty, according to DPJ contacts. Unlike either the budget or the budget-related bills, however, high-level appointments require consent by both Houses, with no recourse to an override by the Lower House. This gives the DPJ and its smaller opposition partners real bargaining power. As recently as two weeks ago, it appeared that the Muto nomination could potentially sail through with bipartisan support. Now the DPJ is threatening to hold the vote hostage to demands for consideration on the budget and the budget-related bills, forcing the government to announce publicly that it is postponing its formal nomination of Muto pending more pressing legislative debates. If Fukuda cannot win over the DPJ, he will have no choice but to find a new nominee, or leave the position temporarily unfilled.

¶12. (C) The Bank of Japan issue is not pure partisan politics. The DPJ party rules call for agreement on high-level appointments by the party's 12-member Executive Board, and several ranking members have already spoken out publicly against Muto, questioning whether a former Ministry of Finance bureaucrat should have control over monetary

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policy, given concerns regarding central bank independence. DPJ contacts tell the Embassy that Ozawa will make the final call, and expect the rank-and-file to follow his lead. Nonetheless, the DPJ's failure to either enunciate criteria for choosing a new nominee or suggest an alternative candidate has left it open to criticism of using the appointment for political gain, at a time when global market conditions require strong leadership at the helm of the Bank of Japan.

New Transparency in Selection Process

¶13. (C) The DPJ has already succeeded in forcing the ruling parties to allow more transparency in the Diet confirmation process. Under the new rules, Muto and the candidates for the two BOJ deputy slots will appear before the Rules Committees of both Houses in open hearings, which will be followed by closed sessions. Both Houses will then vote the nomination up or down in separate plenaries. In the past, when the LDP controlled both Houses, it was not uncommon for nominees to be selected by a handful of party leaders. Diet hearings, if they were held at all, were closed to the public. This time, the LDP has promised to release the transcripts of the question and answer sessions to the public soon after the vote, a sign of the changed circumstances in the divided Diet.

SCHIEFFER